United States Court of Appeals

for the Second Circuit

INTERVENOR'S BRIEF

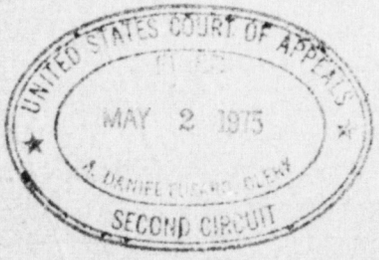
75-4046

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

AMERICAN TELEPHONE AND TELEGRAPH COMPANY,	)	
Petitioner,	)	
v.	)	
FEDERAL COMMUNICATIONS COMMISSION and UNITED STATES OF AMERICA,	)	
Respondents,	)	No. 75-4046
UNITED STATES INDEPENDENT TELEPHONE ASSOCIATION, et al.,	)	
Intervenors.	)	

ON PETITION FOR REVIEW OF ORDER OF
THE FEDERAL COMMUNICATIONS COMMISSION

BRIEF FOR INTERVENOR UNITED STATES INDEPENDENT TELEPHONE ASSOCIATION



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BRIEF FOR
INTERVENOR
UNITED STATES INDEPENDENT
TELEPHONE ASSOCIATION

PRELIMINARY STATEMENT

The interest of Intervenor United States Independent Telephone Association (USITA) in this proceeding is, as set forth in its Motion For Leave To Intervene, the approximately $2.75 million monthly revenue loss by the Independent (non-Bell) telephone companies of the United States resulting from the unlawful action of the Federal Communications Commission

(FCC)[1/] in rejecting tariffs filed January 3, 1975 by American Telephone and Telegraph Co. (A.T.&T.).[2/]

In conformance with the Court's direction to the parties (Preargument Conference Order, April 21, 1975) to avoid duplication and repetition, USITA hereby adopts the "Statement of The Case" and "Argument" contained in A.T.&T. brief; and respectfully submits the following argument in supplement to and in support of the A.T.&T. position.

ARGUMENT

The Commission has neither legal authority nor practical ability to prescribe a rate of return, nor has it done so. Its summary rejection of the January 3, 1975 A.T.&T. tariff filing as "prima facie unlawful" (Order, ¶17; A_____) is therefore itself unlawful and must be set aside.

The Commission Has No Legal Authority To "Prescribe" A Rate Of Return.

To avoid semantic difficulties, we must emphasize at the outset the distinction between a rate of return and

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[1/] Memorandum Opinion and Order, adopted March 4, 1975 (FCC 75-253; A._____ et seq.) ("Order").

[2/] Tariff rates for interstate communications services jointly furnished by A.T.&T. and the Independents are contained in A.T.&T. tariffs. Revenues from jointly provided services are divided among participating companies pursuant to intercompany agreements. The monthly $2.75 million revenue loss represents the difference between the Independents' revenues at the rejected tariff rates and those allowed to become effective on March 9, 1975.

a rate. In utility regulatory parlance a "rate of return" is a percentage figure, which in analyzing the result of utility operations is calculated by dividing rate base (net investment) into net income. Net income, of course is the result of rates (charges) times units of service furnished less expenses. Prospectively, in ratemaking proceedings, "Rate of return in simplest terms is a percentage expression of the cost of capital. It is just as real a cost as that paid for labor, material, and supplies, or any other item necessary for the conduct of the business." A.T.&T., 9 FCC 2d 30, 51 (1967).

Since the Commission ". . . is entirely a creature of Congress, and the determinative question is not what the Board [Commission] thinks it should do but what Congress has said it can do",[3/] respectfully we direct the Court's attention to what Congress has said the FCC can do.

Under the Communication's Act of 1934 (47 U.S.C. 151 et seq.), FCC is authorized, after full opportunity for hearing,

> ". . . to determine and prescribe what will be the just and reasonable charge or the maximum or minimum, or maximum and minimum charge or charges to be

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[3/] CAB v. Delta Airlines, Inc., 367 U.S. 316, 322 (1961).

thereafter observed. . . ." (Section 205(a); 47 U.S.C. 205(a)).[4/] (Emphasis supplied).

When exercised, the power to prescribe is accompanied by an order that the carrier involved ". . . shall not thereafter publish, demand or collect any charge other than the charge so prescribed. . . ." (Ibid.). Prescriptive power is also conferred on the Commission by this same section in respect of classifications, regulations and practices; and under Sections 220(a) and (b) (47 U.S.C. 220(a), (b)) the Commission is authorized to prescribe forms of accounts and records, classes of depreciable property, and depreciation rates.

[4/] The full text of Section 205(a) is:

> "Whenever, after full opportunity for hearing, upon a complaint or under an order for investigation and hearing made by the Commission on its own initiative, the Commission shall be of opinion that any charge, classification, regulation, or practice of any carrier or carriers is or will be in violation of any of the provisions of this Act, the Commission is authorized and empowered to determine and prescribe what will be the just and reasonable charge or the maximum or minimum, or maximum and minimum, charge or charges to be thereafter observed, and what classification, regulation, or practice is or will be just, fair, and reasonable, to be thereafter followed, and to make an order that the carrier or carriers shall cease and desist from such violation to the extent that the Commission finds that the same does or will exist, and shall not thereafter publish, demand, or collect any charge other than the charge so prescribed, as the case may be, and shall adopt the classification and shall conform to and observe the regulation or practice so prescribed." (Emphasis supplied).

"Prescribe", as the context in which it is used in the statute clearly indicates, is not synonomous with "permit" or "allow". Rather, to prescribe is to require, or as Mr. Webster[5/] explains, "Prescribe indicates authoritative dictating or commanding, with explicit clear direction."

Violation of Commission prescribed charges, classifications, practices, regulations, forms of accounts and records, classes of depreciable property and depreciation rates are punishable by forfeiture ($1,000 per day, for violation of Section 205(a)) or fine and imprisonment (not less than $1,000 nor more than $5,000, nor less than one year nor more than three years for violation of Section 220).

These sanctions are convincing of the distinction between "prescribe" and "allow" or "permit". Were the Commission to "allow" a form of account or record, surely imprisonment for use of a different form would be unthinkable.

Mere reading of these sections makes it clear that where the Congress deemed it necessary or appropriate to confer on the Commission prescriptive powers and penalties,

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5/ Third New International Dictionary.

the Congress knew both how and where to do it.[6/] But nowhere in the Communications Act is the Commission empowered to prescribe a rate of return. As the Commission has acknowledged,

> "No specific standards are established in the Communications Act for computing the rate of return. It is subsumed in the statutory standard that rates must be 'just and reasonable' (secs. 201(b) and 205(a)) and in the stated purpose of the act that there be 'adequate facilities at reasonable charges' (sec. 1)." A.T.&T., 9 FCC 2d 30, 52 (1967) (emphasis supplied).

Thus, whether rate of return is viewed as a mathematical result of utility operations or computed for ratemaking purposes as "a percentage expression of the cost of capital," it is clear that the Congress in legislating and the Commission in implementing that legislation have directed their attention to rates and charges, not to the numerous variable cost factors that underlie rates and charges, of which rate of return is but one. And it is to rates and charges that

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[6/] This Court has recently had occasion to review the prescriptive authority of FCC under Section 205, and has specifically observed the nature of that authority, the requirements for its exercise, and the limitations thereon. A.T.&T. v. FCC, 449 F.2d 439 (2d Cir. 1971). The Order here under review heeds none of the Court's admonitions. And as the Court observed in A.T.&T. v. FCC, 487 F.2d 865 (2d Cir. 1973), "We start with the proposition that Congress, rather than purporting 'to transfer its legislative power to the unbounded discretion of the regulatory body,' FCC v. RCA Communications, Inc. 346 U.S. 86, 90 (1953) intended a specific statutory basis for the Commission's authority." (487 F.2d at 872).

the Commission's Section 205 prescriptive powers apply, not to the operating result or cost element called rate of return.

A Rate of Return Cannot Be Prescribed.

That Congress did not authorize FCC to prescribe a rate of return may be due in no small measure to the practical impossibility of performing such a feat.

In keeping with the concept of "prescribe," the objects of prescriptive FCC action detailed in the statute, e.g., charges, regulations, property classes, accounts, depreciation rates, are by their nature both precise and certain, amenable to specific, definitive and enforceable regulatory action.

A rate of return, however, by its nature is an objective, achievable with any degree of precision and at any point in time over time only by fortuitous coincidence of the multiple variables (revenues, expenses, investment) from which it is derived. For "a rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market, and business conditions generally" Bluefield Co. v. Public Service Commission, 262 U.S. 679, 693 (1923). "The law does not contemplate, nor can there be, any guarantee that a particular rate of return, deemed appropriate by the Commission, will actually be earned."

(Re Jamaica Water Supply Co., 89 PUR 3d 119, 120 (N.Y.P.S.C., 1971). Again, "A fair rate of return is a flexible concept and is not related to a static unchanging rule" (Re Rochester Gas & E. Corp., 88 PUR 3d 271, 281 (N.Y.P.S.C., 1971).[7/]

As FCC itself agreed in the same paragraph of its August, 1973 Memorandum Opinion and Order which it now in 1975 footnotes as setting forth its "prescription" of an 8.5% rate of return:[8/]

> "But to the extent that the Trial Staff's argument is to the effect that the filed rates must, under any and all circumstances, produce no more than 8.5%, we cannot agree. For clearly, no revised interstate message toll rate schedule can lay claim to such exactitude in view of the variability or unpredictability of the many economic factors that operate over any period of time to produce the level of interstate earnings" (A.T.&T., 42 FCC 2d 293, 300 (1973)).

[7/] See also Washington Gas Light Co. v. Baker, 188 F.2d 11 (D.C. Cir. 1950) where the court found error in a rate of return finding possibly based on a finding in some prior proceeding. The Court there stated: There is nothing before us to indicate that pertinent local conditions and economic conditions generally have remained static during the intervening years. Nor does it appear that the risk factor, so important an element in fixing rate of return, has remained static" (188 F.2d at 17).

[8/] Other than this footnote reference, the Commission cites no other basis for its 1975 claim that in 1972 it prescribed a rate of return.

In the face of this recognition of reality by the Commission, could it be seriously argued that A.T.&T. should not be subjected to a Section 205(b) forfeiture of $1,000 a day for each day since the alleged 1972 "prescription" of an 8.5% rate of return that did not "thereafter publish, demand or collect" an 8.5% rate of return?[9/] The patent absurdity of such a result suggests the equal absurdity of the claim now that the Commission in fact prescribed a rate of return in 1972. Using the Commission's own conclusion that "Rate of return in simplest terms is a percentage expression of the cost of capital," can the Commission seriously believe or even contend that it can require A.T.&T. to pay precisely 8.5%, no more, no less, for the capital needed to conduct its business?

In short, a rate of return simply cannot be prescribed, any more than it can be guaranteed to a utility by regulatory authority or "thereafter observed"[10/] by a common carrier. The Order cites no precedent for its novel theory, nor are we aware of any. And although in view of the foregoing the Court need not reach the point, the Commission's claim now in 1975 that it prescribed an 8.5% rate of return in 1972 is somewhat less than supportable.

9/ The Order (¶19; A._____) notes that A.T.&T.'s 1974 rate of return was 8.53%, but was only 7.89% in the last quarter.

10/ Section 205(a), 47 U.S.C. 205(a).

The Commission's 1972 Decision Did Not Prescribe A Rate Of Return.

The Commission did not, in fact prescribe an 8.5% rate of return or any other rate of return, either in 1972 or at any other time. Only brief reference to the 1972 decision (38 FCC 2d 213) is needed to demonstrate this point.

In its 1972 decision, the Commission's "Conclusions on Rate of Return" are set forth in four paragraphs (104-107; 38 FCC 2d at 244-246). Neither the word nor the concept of "prescription" is present. Indeed, the 1975 characterization of that decision as having "prescribed" an 8.5% rate of return appears to have come as a surprise to at least two of the current Commissioners who participated in the 1972 case (See Statements of Commissioners R. E. Lee and Hooks, A._____), and may have come as a shock to two former Commissioners who dissented in the 1972 case. (Three members of the 1975 Commission were not on the 1972 Commission).[11/] Former Commissioner Johnson, dissenting, characterized the 1972 decision as "While purporting to set an 8.5% rate of return, Bell is told that if it earns 9.0% that, too, will be approved. There is no telling how high it can go before FCC will be concerned" (38 FCC 2d at 270). Commissioner H. R. Lee, dissenting, observed that "The majority's specification of a range of 8.5

11/ The situation here is analagous to the expression of views by one Congress as to construction of a statute enacted by an earlier Congress, views which are generally accorded little, if any, significance. See, e.g., U.S. v. Southwestern Cable Co., 392 U.S. 157, 170 (1968).

to 9.0 percent appears to foreclose appropriate Commission action if earnings of A.T.&T. within that range should result from factors other than efficiencies and productivity gains" (38 FCC 2d at 279). Both dissents are wholly inconsistent with the new 1975 prescription theory. Moreover, in the context of the dissents, it is a fair assumption that neither would have been written if the 1972 decision had indeed prescribed an 8.5% rate of return.

What the Commission actually found in the 1972 decision was "that the minimum rate of return that Bell should be permitted to earn on its interstate operations at this time is 8.5%. . . ." (¶107; A._____ (emphasis supplied)). Additionally, the Commission "specified a range of 8.5% - 9.0% as the range of reasonableness for the earnings of Bell. . . ." (Ibid.)

Further doubt as to the nature of the Commission's 1972 rate of return determination, if any remains, is removed by reference to the Commission's rulings on exceptions to its 1972 order (A.T.&T., 38 FCC 2d 492 (1972). There the Commission again and again specifically characterized its 1972 rate of return finding as "a minimum level of interstate earnings of 8.5% would be just and reasonable" (A.T.&T., 38 FCC 3d 492, 493 - CWA Exception 5); ". . . the minimum allowable rate of return . . . is 8.5%" (Id., at 494 - UTS Exception

8); "We allow a minimum return of 8.5% on Bell's total interstate and foreign operations" (Id., at 495 - USITA Exception 9). "The record supports the conclusion that Bell is entitled to a minimum return of 8.5%" (Ibid. - DOD Exception 5); ". . . we find the minimum allowable return to be 8.5%" Ibid. - Chicago Exception 3); ". . . the minimum 8.5% return we allow" (Id., at 496 - GTE Exception 16); "Record supports minimum overall return allowance of 8.5%" (Id., at 498 - Bell System Exception 90) (emphasis supplied).

Given this repeated and specific characterization of its 8.5% finding as the minimum allowable rate of return on what basis does the Commission now in 1975 purport to convert "minimum allowable" into "prescribed maximum," requiring rejection of rates designed to produce a return above the "minimum allowable"?

Not surprisingly, FCC found no basis for its newly discovered "prescription" in the 1972 decision itself, and it cites none. Rather, the Commission now recites that on the 1972 record it determined the cost of debt and equity for A.T.&T. and established the appropriate rate of return required to cover those costs. From these facts, the Commission then concludes that "This action was a properly determined prescription of Bell's rate of return" (Order, ¶16; A._____). Despite this conclusion, how a rate of return allowance now becomes a prescription remains unexplained, except perhaps by the theory of ipse dixit. Surely more is required, yet the Order offers none.

There is indeed a footnote reference at that point in the Order to a page in an August, 1973 order (42 FCC 2d 293, 300) on which the Commission, in rejecting its Trial Staff's contention that A.T.&T. tariff filings might result in earnings in excess of the $145 million authorized by the Commission, referred to "the 8.5 - 9.0% range of reasonableness prescribed by that decision." (42 FCC 2d at 300). Again, in the same paragraph, appears reference to ". . . our prescription of 8.5 - 9.0% as the range of reasonableness."

In addition to the obviously imprecise and inaccurate use of the words "prescribed" and "prescription",12/ however, the Court will note that the 1973 reference is to a range, not to a prescribed 8.5% maximum, with that range being further described (still in the same paragraph) as "Essentially . . . intended as our criteria for measuring the reasonableness of A.T.&T.'s interstate rates and earnings and the need for adjustment therein." "Adjustment" was thus

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12/ The mere recitation of the word "prescribe", even if properly addressed to "charges", is clearly insufficient to constitute a legally binding prescription. For Section 205(a) requires specific findings of unlawfulness of an existing rate, and contemplates issuance of a cease and desist order and a command that the rate prescribed shall be thereafter observed. The 1973 order merely recites the word. It meets none of the statutory requirements.

anticipated, not prohibited, and nothing in the 1973 order or in the 1972 order, either expressly, by implication, or by interpretation, can be said to require prior Commission approval of the filing of new interstate rates by A.T.&T.

CONCLUSION

In context, then, it is clear that the Commission did not prescribe a rate of return to be thereafter observed by A.T.&T. Indeed, the Commission has no authority to do so, nor is a prescribed rate of return a real-world possibility. The Commission's rejection of the January 3, 1975 A.T.&T. tariff filing, being based solely on its novel theory of a prior rate of return prescription, is therefore an unlawful action and must be vacated.

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CERTIFICATE OF SERVICE

I, Carl S. Rowe, a member of the Bar of this Court certify that I served two copies of the attached Brief of Intervenor United States Independent Telephone Association this 2nd day of May, 1975, by mail, postage prepaid, on the Petitioner, the Federal Communications Commission, the United States of America, and each Intervenor in this proceeding, as set forth on the attached list.

Additionally, pursuant to the Court's Preargument Conference Order, copies of this Brief have this day been hand delivered to Petitioner's office Room 710, 2000 L Street, N.W., Washington, D.C.

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